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Department of the Treasury
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Person To Contact:

Telephone Number:

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Legend

Entity E =

State S =

Plan =

Dear

This responds to your authorized representative's letter and subsequent correspondence, on behalf of Entity E and its section 457(b) Plan, requesting a ruling concerning the proposed amended and restated deferred compensation plan (the "Plan"). Entity E intends the Plan to be an eligible deferred compensation plan under section 457(b) of the Internal Revenue Code of 1986 (the "Code"), as amended under the Economic Growth and Tax Relief Reconciliation Act of 2001 ("EGTRRA") and under subsequent legislation. The Plan was adopted by Entity E, which is represented to be an eligible local governmental employer in State S as described in section 457(e)(1)(A) of the Code.

Under the Plan, a participant may elect to defer compensation that would have been received for services rendered to Entity E in any taxable year until death, severance from employment, attainment of age 70½, or until the occurrence of an unforeseeable emergency.

The Plan also permits Entity E to establish a program to allow participants to take loans from their plan accounts, subject to certain restrictions. Loans made under the Plan are subject to rules in the Plan and in

§ 1.457-6(f)(2) of the Income Tax Regulations, including provisions restricting the maximum amount and term of a plan loan.

A participant's election under the Plan to defer compensation not yet paid must be filed prior to the beginning of the month in which the compensation to be deferred is paid or made available. The Plan provides for a maximum amount that may be deferred by a participant in any taxable year and also provides for a catch-up computation for amounts deferred for one or more of the participant's last three taxable years ending before the participant attains normal retirement age under the Plan.

The Plan also provides for the age 50 catch-up contributions described in section 414(v) and in § 1.457-4(c)(2). However, the Plan provides that a participant can only utilize one of the two catch-up contribution provisions during a single year. The amounts that may be deferred under the annual maximum limitation and the catch-up provisions are within the limitations of section 457, including the section 457(c) coordinated deferral provision.

With certain limitations, participants or beneficiaries may elect the manner in which their deferred amounts will be distributed. The Plan provides that the manner and time of benefit payout must meet the distribution requirements of section 401(a)(9) of the Code.

The Plan provides that amounts of compensation deferred thereunder are to be transferred to and held in a trust described in section 457(g)(3) for the exclusive benefit of the participants, their beneficiaries and alternate payees. All amounts deferred under the Plan must be transferred to the appropriate trust within a short period after such compensation would otherwise have been paid. The rights of any participant or beneficiary to payments pursuant to the Plan are generally nonassignable and not subject to pledge, attachment, or encumbrance.

All amounts deferred under the Plan are vested immediately in the participants' accounts, and no amount is subject to a substantial risk of forfeiture. In addition, Entity E's employees are subject to social security and Medicare taxes upon their wages because Entity E is covered by an agreement entered into by State S pursuant to section 218 of the Social Security Act.

Section 457 of the Code provides rules for the deferral of compensation by an individual participating in an eligible deferred compensation plan as defined in section 457(b).

Section 457(a)(1)(A) of the Code provides that for a participant in an eligible governmental deferred compensation plan, "[a]ny amount of compensation deferred under the plan, and any income attributable to the

amounts so deferred, shall be includible in gross income only for the taxable year in which such compensation or other income" is paid to the participant or beneficiary.

Section 457(b)(5) prescribes that an eligible deferred compensation plan must meet the distribution requirements of section 457(d).

Section 457(d)(1)(A) provides that for a section 457 plan to be an eligible plan, the plan must have distribution requirements providing that under the plan amounts will not be made available to participants or beneficiaries earlier than i) the calendar year in which the participant attains age 70½, ii) when the participant has a severance from employment with the employer, or iii) when the participant is faced with an unforeseeable emergency as determined under Treasury regulations.

Section 457(e)(1)(A) defines an eligible employer to be a State, political subdivision of a State, and any agency or instrumentality of a State or political subdivision of a State.

Section 457(g) provides that a plan maintained by an eligible governmental employer shall not be treated as an eligible deferred compensation plan unless all assets and rights purchased with such deferred compensation amounts and all income attributable to such amounts, property, or rights of the plan are held in trust for the exclusive benefit of participants and their beneficiaries. Section 457(g)(3) provides that custodial accounts and contracts described in section 401(f) shall be treated as trusts under rules similar to the rules under section 401(f).

Section 3101(a) imposes Federal Insurance Contributions Act ("FICA") taxes on the income of every individual in an amount equal to a percentage of the wages received with respect to employment. Section 3111(a) provides that the employer portion of FICA tax is imposed directly upon the employer as an excise tax on wages paid to employees in its employ. Similarly, section 3301 provides that Federal Unemployment Tax Act ("FUTA") taxes are imposed on every employer as an excise tax on wages paid to employees in its employ.

Section 3121(a) provides that for FICA purposes, with certain exceptions, that the term "wages" means "all remuneration for employment." Section 3121(a)(5) excludes from the definition of wages certain qualified retirement plans and tax favored annuities for FICA purposes, but does not exclude arrangements described in section 457(b).

Wages are generally subject to FICA tax when they are actually or constructively paid. Section 31.3121(a)-2(a) of the Employment Tax and Collection of Income Tax at Source Regulations (Employment Tax Regulations). However, section 3121(v)(2)

provides a special timing rule for deferrals under a nonqualified deferred compensation plan.

Section 3121(v)(2) provides that any amount deferred under a nonqualified deferred compensation plan shall be taken into account for FICA purposes as of the later of when the services are performed, or when there is no substantial risk of forfeiture of the rights to such amounts. Under § 31.3121(v)(2)-1(2)(ii)(A) of the Employment Tax Regulations, an amount deferred under a nonqualified deferred compensation plan that is not subject to a substantial risk of forfeiture is required to be taken into account as wages for FICA tax purposes on the date when the services are performed creating the legal right to the deferred compensation. For the participants in Entity E's Plan, the deferred amounts are taken into account for FICA tax purposes when their services are performed because the deferred compensation is immediately vested in their accounts.

Section 3121(v)(2)(C) provides that the term "nonqualified deferred compensation plan" means any plan or other arrangement for the deferral of compensation other than a plan described in section 3121(a)(5). Under section 3121(v)(2)(B), any amount taken into account as wages under section 3121(v)(2)(A) and attributable income thereto, is not subsequently treated as wages for FICA tax purposes.

Under I.R.S. Notice 2003-20, 2003-1 CB 894, a section 457(b) plan is treated as a nonqualified deferred compensation plan subject to the special timing rules contained in section 3121(v)(2). Section 31.3121(v)(2)-1(b)(1) of the Employment Tax Regulations defines the term "nonqualified deferred compensation plan" as any plan or other arrangement, other than a plan described in section 3121(a)(5), that is established by an employer for one or more of its employees, and that provides for the "deferral of compensation." A plan provides for the deferral of compensation with respect to an employee only if, under the terms of the plan and the relevant facts and circumstances, the employee has a legally binding right during a calendar year to compensation that has not been actually or constructively received and that, pursuant to the terms of the plan, is payable in a later year. Section 31.3121(v)(2)-1(b)(3) of the Employment Tax Regulations.

A nonqualified deferred compensation plan "is established on the latest of the date on which it is adopted, the date on which it is effective, and the date on which the material terms of the plan are set forth in writing." Section 31.3121(v)(2)-1(b)(2)(i) of the Employment Tax Regulations.

Based upon the provisions of the Plan summarized above and the documents presented, we conclude as follows:

1. The proposed amended and restated Plan constitutes an eligible deferred compensation plan as defined in section 457(b) of the Code, as amended under EGTRRA.
2. Under section 457(a)(1)(A), amounts of compensation deferred under the Plan, including any income attributable to this deferred compensation, will be includible in the recipient's gross income only for the taxable year or years in which amounts are paid to a participant or beneficiary under the terms of the Plan.
3. Under section 3121(v)(2), amounts deferred under Entity E's plan are required to be taken into account for purposes of FICA taxes when the participant's services giving rise to the legal right to deferred compensation are performed.

No opinion is expressed concerning the timing of the inclusion in income of amounts deferred under any deferred compensation plan other than the above-described Plan.

This ruling is directed only to the Plan and not to any other section 457(b) plan, and it applies only if Entity E amends the Plan submitted on November 21, 2006 by adopting the revisions submitted on May 15, 2007. Section 6110(k)(3) of the Internal Revenue Code provides that this ruling may not be used or cited as precedent.

Sincerely,

Cheryl Press
Senior Counsel, Qualified Plans Branch 2
(Employee Benefits)
(Tax Exempt & Government Entities)

Enclosure (1)